No. 20,876

IN THE

United States Court of Appeals

For the Ninth Circuit

JOHNNY R. AUSTAD and DOROTHY AUSTAD, his wife,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANTS' OPENING BRIEF

ARTHUR H. TIBBITS,
55 New Montgomery Street,
San Francisco, California 94105.

MESCH, MARQUEZ & ROTHSCHILD,
239 North Church Avenue,
Tucson, Arizona 85701,

Attorneys for Appellants Johnny R. Austad and Dorothy Austad, his wife.

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I

STATEMENT OF JURISDICTION

This is an appeal from a final judgment in favor of Appellee, United States of America, rendered by the United States District Court for the District of Arizona in an action by the Appellee for foreclosure of a mortgage held by the Small Business Administration, a federal agency, and upon a written guaranty for payment of a note. Jurisdiction was based upon the provisions of 28 USC 1345. Jurisdiction of this Court is invoked under the provisions of 28 USC 1291 and 1294. A timely Notice of Appeal was filed on

January 31, 1966, within thirty (30) days after entry of judgment on January 11, 1966 (CTR[1] 84-93).

II

STATEMENT OF THE CASE

A. The Nature of the Controversy.

On December 10, 1964, Appellee, United States of America, filed its civil action against the Appellants, Johnny R. Austad and Dorothy Austad, his wife, and other parties including the Austad Steel Co., Inc., a bankrupt, to foreclose a mortgage executed by the Austad Steel Co., Inc., an Arizona corporation, the mortgagor, in favor of the Small Business Administration, a federal agency, the mortgagee, to secure payment of the former's promissory note, the unpaid balance of which then amounted to $165,992.91 together with interest, expenses and costs of suit, and to recover on a written guaranty executed by the Appellants in favor of the Appellee, dated December 17, 1958, guaranteeing the unconditional payment of said note when due. Said mortgage and note were entered into on December 17, 1958. The mortgagor, Austad Steel Co., Inc., defaulted on its monthly installment due September 17, 1959, and on June 20, 1960 was adjudicated bankrupt (CTR 2-21).

By their Amended Answer, the Appellants admitted substantially all the factual allegations of the Com-

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[1]Parenthetic references preceded by "CTR" are to the Clerk's Transcript of Record.

plaint, including execution of the mortgage and note by Austad Steel Co., Inc., their written guaranty of said note, the default of Austad Steel Co., Inc., on December 17, 1959, and the adjudication of bankruptcy of Austad Steel Co., Inc., on June 20, 1960, but they denied that any demands were made upon them for payment of the balance due under the note until filing of this action December 10, 1965, approximately five (5) years and three (3) months after the note became due and payable, and additionally raised four affirmative defenses (CTR 63-64):

1. Appellee failed to bring this action on the indebtedness within sixty days after demand by Appellants therefor as required by Arizona Statute (Arizona Revised Statutes §§12-1641 and 12-1646);

2. Appellants were released under their written guaranty by Appellee's action in repeatedly waiving principal payments when due and accepting only interest payments on the obligation;

3. Appellee was barred by laches from prosecuting its action there having elapsed a period of approximately five (5) years and three (3) months from the date of default and the filing of its Complaint; and

4. Appellee was estopped to recover on Appellants' written guaranty because of its willful and unconscionable delay in bringing this action from the date of default, September 17, 1959, and the date of filing of its Complaint, December 10, 1964, a period of approximately five (5) years and three (3) months, which delay greatly diminished the value of the se-

curity for the note causing irreparable harm to the Appellants.

Appellants attached to their Amended Answer a copy of a letter from J. R. Austad to the Small Business Administration dated September 19, 1961, in which demand was made to bring an action on the note and mortgage immediately.

On July 21, 1965, Appellee moved for Judgment on the Pleadings (CTR 57-59) which was granted as to these Appellants on August 2, 1965 (CTR bet. 67 and 68). A Judgment and Decree of Foreclosure was entered on January 11, 1966, against Appellants Johnny R. Austad and Dorothy Austad and also against the Austad Steel Co., Inc., in the total amount of $213,092.50, together with interest thereon (CTR 84-92).

B. Questions Involved.

1. Were the Appellants released on their written guaranty by the failure of the Appellee to bring an action on the indebtedness within sixty (60) days after demand by them to do so?

2. Was the Appellee estopped from bringing this action on the ground of laches?

3. Were the Appellants discharged on their written guaranty by Appellee's willful destruction and impairment of the security?

4. Were there questions of fact raised by Appellee's Complaint and Appellants' Amended Answer which would prevent entry of a judgment upon a motion for Judgment on the Pleadings?

C. Specifications of Errors.

1. The District Court erred as a matter of law in holding that Appellee had not released Appellants on their written guaranty by failing to bring an action on the indebtedness within sixty (60) days after demand by them to do so.

2. The District Court erred as a matter of law in holding that Appellee was not estopped from bringing this action on the ground of laches.

3. The District Court erred as a matter of law in holding that Appellants were not released on their written guaranty by Appellee's willful destruction and impairment of the security.

4. The District Court erred as a matter of law in entering a Judgment and Decree of Foreclosure as to these Appellants on Appellee's motion for Judgment on the Pleadings where factual issues were raised by the pleadings.

III

ARGUMENT

A. APPELLANTS WERE RELEASED ON THEIR WRITTEN GUARANTY BY THE FAILURE OF THE APPELLEE TO BRING AN ACTION ON THE INDEBTEDNESS WITHIN SIXTY DAYS AFTER DEMAND BY THEM TO DO SO.

Under Arizona law, sureties and guarantors under written contracts for the payment of money have a right to require by notice in writing that the creditor or obligee bring an action under the contract forthwith, and if the creditor or obligee fails to bring such action the surety or guarantor giving such notice will be discharged from all liability thereon.

Arizona Revised Statutes §12-1641 reads as follows:

> "Action by creditor; failure to bring action and effect
>
> Any person bound as surety upon a contract for payment of money or performance of an act, when the right of action has accrued, may require, by notice in writing, the creditor or obligee forthwith to bring an action upon the contract. If the creditor or obligee, not being under legal disability, fails to bring the action within sixty days after receiving the notice, and prosecute it to judgment and execution, the surety giving the notice shall be discharged from all liability thereon."

Arizona Revised Statutes §12-1646 extends this remedy to guarantors as well as sureties.

On a motion for Judgment on the Pleadings, all well pleaded material allegations of the opposing parties' pleadings are to be taken as true, and all allegations of the moving party which have been denied are taken as false.

> *Wyman v. Wyman,* CA 9, 109 F.2d 473;
> 2 Moore's Federal Practice 2269, Para. 12.15 and other cases cited in footnote 7.

On an appeal from a Judgment entered on such a motion this Court must accept the allegations of the Appellants in their Amended Answer as true, to wit: Appellee failed to bring an action on the indebtedness within sixty (60) days following demand by Appellants to do so. As stated in *Phenix v. Bijelich,* 30 Nev. 257, 269, 95 P. 351, 353, cited by the Ninth Circuit Court in *Wyman v. Wyman,* supra:

> "When a party moves for judgment on the pleadings, he not only for the purposes of his motion admits the truth of all the allegations of his adversary, but must also be deemed to have admitted the untruth of all his own allegations which have been denied by this adversary."

Appellants did not waive their rights under the above cited Arizona statutory provisions (Exhibit C, CTR 21) and any such attempted waiver would have been null and void as against public policy, since such statutory provisions are enacted to protect debtors from oppression. This result has been reached under similar statutory provisions in California, viz: California Code of Civil Procedure §726 providing for one form of action to recover on a debt secured by a mortgage, and California Civil Code §2924(c) providing for a three-month period after default in which time the creditor may reinstate the loan, and is so expressed in California Civil Code §2953.

Tomczak v. Ortega, 240 CA 2d 902;

Altman v. McCollum, 107 CA 2d Supp. 847.

The law on this point has been summarized in 34 Cal. Jur. 2d at pages 102-103:

> "The statute [C.C.P. §726] providing for but one form of action to recover any debt or enforce any right secured by a mortgage was enacted to promote the public welfare by protecting debtors from oppression. It must be construed as declaring public policy of the state and cannot be waived by contract. A provision in a trust deed waiving the benefit of this provision is inconsistent with the purpose of the entire instrument

> and attempts to destroy its legal effect as a trust deed. . . . This general understanding is now incorporated in a statute [CC §2953] that provides that an express agreement whereby a borrower, at the time of or in connection with the making or renewing of any loan secured by a trust deed, mortgage, or other instrument creating a lien on real property, agrees to waive the rights or privileges conferred on him by various code sections, including the one under consideration, is void and of no effect."

Accordingly, when the Appellee failed to bring an action on the indebtedness within sixty days following demand by Appellants that it do so, the Appellants were discharged from all liability thereon.

B. APPELLEE IS ESTOPPED FROM BRINGING THIS ACTION BECAUSE OF LACHES

Appellants specially pleaded the defense of laches in their Amended Answer (CTR 63, 64). Laches has been defined as an inexcusable delay in asserting a right, and entails (1) an unreasonable delay and (2) prejudice to the defendant.

> *Tovrea Land and Cattle Company v. Linsenmeyer,* 100 Ariz. 107, 412 P.2d 47, 64;
>
> *Barr v. Petzhold,* 77 Ariz. 399, 273 P.2d 161, 165;
>
> *Price v. Sunfield,* 57 Ariz. 142, 112 P.2d 210, 212;
>
> *Hamud v. Hawthorne,* 52 C.2d 78;

King v. Los Angeles County Fair Assn., 70 CA 2d 592, 596;

30A Corpus Juris Secundum, "Equity", §§112 et seq.;

Witkin, California Procedure, "Pleading", §490;

Witkin, Summary of California Law, "Equity", §§ 12, 13.

In *Barr,* supra, the Arizona Supreme Court stated at p. 165:

> "This Court recognizes as meritorious the defense of laches. The general rule is that a plaintiff must exercise diligence and avoid unreasonable delay in prosecuting an action. The reason for this rule is that unreasonable delay and lack of diligence either evidence an abandonment by the plaintiff of his claim or else prejudice in some way the defense against such claim."

Laches may bar relief in equity irrespective of whether the Statute of Limitations has run on the action at law.

Alger v. Brighter Days Mining Corp., 63 Ariz. 135, 160 P.2d 346, 352.

In *Alger,* supra, the Court held that a minority stockholder was guilty of laches though the suit was brought *after three years* and within the Statute of Limitations because of prejudice to the defendant corporation stating at pp. 349 and 352:

> "Plaintiffs stood by and refrained for more than three years before any legal action was commenced by them during which period large sums

> of money had been expended upon the property by Brighter Days, and numerous persons had purchased stock in the new company."
>
> * * *
>
> "It is well settled that a minority stockholder may lose his right to sue or defend on behalf of the corporation if unreasonably delaying, with knowledge of the facts, to bring suit."

In *King,* supra, *a delay of two years* was sufficient to justify a refusal to set aside a transfer of assets of a nonprofit corporation. And in *Hamud,* supra, plaintiff mortgagors gave a quitclaim deed to permit strict foreclosure on default, and then *after 5 years* sought to have the deed declared a mortgage. The Court denied relief because they had waited too long and there had been a change in the circumstances (interest of oil company in property) in the meantime.

On this Appeal the following facts must be accepted as true: The Appellee wilfully delayed filing its action for approximately five (5) years and three (3) months during which time the security for the note greatly diminished, causing Appellants irreparable harm. [See Appellants' Amended Answer, CTR 63-64; Complaint, First Cause of Action, Para. IX, CTR 5, Clerk's Docket Entries CTR 77, and pages 6 and 7 of this Brief, supra.] Accordingly, if these facts are so, it is submitted that this action is barred from prosecution by reason of laches.

Appellee contended below, however, that the defense of laches was not applicable against the United States as the result of any action or inaction of its agents or

employees in an action of this sort. *But this applies only when the United States is acting in its governmental capacity. When it acts in a proprietary capacity or enters into contractual relationships an estoppel may be asserted against it provided the functions of government are not impaired thereby.*

U.S. v. New Orleans Pac. Ry. Co., 248 U.S. 507;

La Republique Francaise v. Saratoga Vichy Spring Co., 191 U.S. 427;

U.S. v. Bank of America, D.C. Cal., 47 F. Supp. 279;

City of Los Angeles v. County of Los Angeles, 9 C.2d 624;

30A Corpus Juris Secundum, "Equity", §114, and cases cited in footnote 35;

27 American Jurisprudence 2d "Equity", §156.

In *La Republique Francaise* the government of the French Republic sued to enjoin use of the name "Vichy". The defense of laches was asserted on the ground that the French government had done nothing for thirty years to protect its interest in this name. The Court held that this defense was applicable to the French government where they were acting for the protection of a *private and proprietary interest.* Quoting from the Court's opinion at page 438:

> "In such cases either where the government is suing for the use and benefit of an individual or for the prosecution of a private and proprietary, instead of a public or governmental right, it is clear that it is not entitled to the exception of

> *nullum tempus,* and that the ordinary rule of laches applies in full force." (Cases cited)

And in *U.S. v. Bank of America,* supra, the United States delayed almost 2½ years before notifying banks which had collected checks on forged endorsements. The Court, Judge Roche, entered judgment for the defendant holding that the defense of laches was applicable to the government when engaged in private commercial activities, stating at page 281:

> "Even if neither of the foregoing theories were applicable the Government might well be barred by its long delay in notifying the defendants after discovery of Howlett's fraud. When the United States issues commercial paper it does so on the same basis as any individual and with no special privileges. Cooke et al. v. United States, 91 U.S. 389, 398, 23 L.Ed. 237. And while it will not be bound by the state statute of limitations, like any other litigant it may be guilty of laches. (Cases cited) Laches is a valid defense if the delay appears to have prejudiced the defendant."

The case of *United States v. Summerlin,* 310 U.S. 414 cited by Appellee below (CTR 59) involved a claim assigned to the Federal Housing Administrator *in its governmental capacity, and not in its proprietary capacity.* The right asserted here however involves the foreclosure of a mortgage and collection of a note arising out of the government's activities through the Small Business Administration an executive agency of the United States (CTR 2-21) engaged in the business of making loans to private individuals

and corporations. 15 USC §661; *First Louisiana, Inc., Corp. v. U.S.,* 5 CA 1965, 351 F.2d 495. These activities clearly show that *the government was acting here in a private and proprietary and not in a governmental capacity,* just as it and the French Republic were acting in the cases above cited. Accordingly the defense of laches would be equally applicable to it as to any individual.

C. APPELLANTS HAVE BEEN RELEASED FROM THEIR WRITTEN GUARANTY BY REASON OF APPELLEE'S WILLFUL IMPAIRMENT OF THE SECURITY.

Where a creditor does an act or fails to perform an act whereby injury or loss accrues to the surety without his assent, the surety is entitled to be discharged.

Roberts v. Security Trust & Savings Bank, 196 C. 557;

46 Cal. Jur. 2d 256, 257, "Suretyship and Guaranty".

So in the instant case, where Appellee by its inaction over a period of approximately five (5) years and three (3) months willfully permitted the security to greatly depreciate in value without the assent of the Appellants, the latter are entitled to be discharged from their written guaranty.

Appellee contended below that by the terms of the written guaranty Exhibit "C" to the Complaint (CTR 21) Appellants had conferred upon the Small Business Administration full power in its uncontrolled dis-

cretion and without notice to them to deal in any manner with the security (CTR 57-59). However, this did not give it the right to destroy or diminish the value of the security *by any willful act or willful failure to act*. The written guaranty in this connection provides as follows (CTR 21):

> "The obligations of the undersigned hereunder and the rights of SBA in the collateral, shall not be released, discharged, or in any way affected, . . . by reason of any deterioration, waste, or loss by fire, theft or otherwise of the collateral *unless such deterioration, waste, or loss be caused by the willful act or willful failure to act of SBA*" (emphasis supplied).

Accordingly by the very terms of the written guaranty to which SBA is bound as a party, the Appellants have been released therefrom because of SBA's willful destruction of the security.

D. THE PLEADINGS RAISED FACTUAL ISSUES WHICH PREVENTED ENTRY OF JUDGMENT ON THE PLEADINGS.

It is well established that a plaintiff may not move for judgment on the pleadings where the Complaint and Answer raise issues of fact which if proved would defeat recovery.

Caterpillar Tractor Co. v. International Harvester Co., CA 9, 1939, 106 F.2d 769;

2 Moore's Federal Practice, 2268-2270, Para. 12.15 and cases cited in footnote 12.

In the instant case Appellee's Complaint (CTR 2-21) and Appellants' Amended Answer (CTR 63-64) raised the following factual issues:

1. Did Appellants make demand upon Appellee to bring an action on the note on or about September 19, 1961?

2. Did Appellee fail to bring an action on the indebtedness within sixty days following said demand?

3. Did Appellants make repeated demands on the Appellee to exercise its rights with dispatch?

4. Did Appellee willfully delay bringing its action for approximately five (5) years and three (3) months?

5. Did Appellee's willful delay in bringing its action for approximately five (5) years and three (3) months greatly diminish the value of the security for the loan causing irreparable harm to Appellants?

Any or each of the foregoing factual issues if proved would have defeated recovery by the Appellee on its Complaint as against these Appellants in the light of the principles of law set forth hereinabove under headings "A", "B", and "C". Accordingly the Judgment entered below on Appellee's Motion for Judgment on the Pleadings was not authorized under Rule 12 (c) of the Federal Rules of Civil Procedure and should be reversed.

CONCLUSION

It is respectfully submitted, for each of the reasons hereinabove set forth, that the judgment entered in favor of Appellee and against Appellants be reversed and the action remanded for further proceedings in the District Court.

Dated, San Francisco, California,
February 6, 1967.

Respectfully submitted,
ARTHUR H. TIBBITS,
MESCH, MARQUEZ & ROTHSCHILD,
By ARTHUR H. TIBBITS,
Attorneys for Appellants Johnny R. Austad and Dorothy Austad, his wife.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ARTHUR H. TIBBITS,
Attorney for Appellants.